News Flash

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General information about Offshore companies in Hungary

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Nowadays, the term “offshore” demonstrates a negative expression mostly given to the tax dodger companies, rather than a legal term. Although basically most of these companies are operating legally secure and transparent, the tax evasion scandals in the recent years left the mark of prejudice especially on those who had been established in exotic countries. It is important to mention, that these offshore locations not necessarily appealing because of their favorable tax structure, but rather the anonymity , complete discretion what they are offering and the unavailability in spite of official request. The latter feature is what became less and less relevant in the recent years, because nowadays there is barely any “offshore” state who did not take part in any data exchange treaty. There are several reasons why these companies are operating and we are going to cover these details, conditions and restrictions in our current, short newsletter.

What is a tax haven?

Although this concept legally does not exist, tax haven is a country, state or territory offering little or no tax liability to foreign individuals and businesses registered domestically, but operating outside of its border.

What are the benefits?

We can classify the benefits to two main categories:

- **By advantages of taxation**:

  The companies can make tax savings provided by the registered country tax reduction schemes.

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- **With advantages regardless of taxation, by associated benefits:**

  Companies can get into favorable position by not only by taxation aspect, but by independent factors, such as foreign exchange rate losses, savings on accounting fees with no obligation to bookkeeping,

Why is it profitable for the registering countries?

States who are offering these tax advantages are usually have low population and small territory, their main economic income comes from tourism and other services so they can gain significant profit from these offshore businesses, since their collected revenue not only comes from taxes but the law firms, representatives and banks necessary for these companies creating new jobs for local people.

What are the advantages?

Although people often thinks that these offshore companies completely exempt from tax, despite the favorable conditions, this is not true. Even though there are states where they always have an annual fee, but the income is tax free, while there are countries where subscribed capital is the tax basis not the income. Furthermore, there are states where companies are taxed by their net gain with a reduced amount.

What are the restrictions?

- **Related to the members:**

  1. Quantitative restrictions: For example, in Panama at least three directors necessary for establishing/operating a company.
  2. Ethnic restrictions: For example, in Liechtenstein at least one director must be a local citizen.

- **Related to currency:**

  This restriction is mainly in force in countries with unstable national currency, most of popular offshore zones are exempt from foreign exchange restrictions.

- **Related to director meetings:**

  In general this restriction is not too common, but there are some states prescribed that the annual director meetings must be held domestically for the purpose of promoting tourism.

- **Related to bank accounts:**

  This isn't too a common either, but some states whom specified in law that the domestically founded companies must open bank account in local banks.

The Hungarian situation

In the last years the interest in offshore companies had a fallback due to the fact that many European States, including Hungary, introduced restrictive provisions related to these controlled foreign companies (CFC). These new regulations took these incomes under a far more disadvantageous taxation and they now fall into a much worse position than revenues from normal taxed domestic and foreign companies. According to the Hungarian provisions in force, undistributed profits in controlled foreign companies got consolidated under taxation too and the eligibility of considerations allocated to foreign companies are subjected to strict conditions. Furthermore there are more aggravations too for example, that impairments shall not be recorded for the shares in the CFC, that dividends received from the CFC shall not be counted as a tax base reducing item and that the advantages relating to the announced share cannot be applied to these companies.
It is also important, that applicants can fall under unfavorable treatment in public procurements if there is a controlled foreign company among its owners.

On the whole

In taxation it's a general legal principle, that tax-payers are not obligated to have greater tax burden if there is a legal alternative to a lower one. Therefore, if a company considering creating strategy in the aspect of tax planning, it is completely legal to choose that alternative what offers the lower tax burden and tax rate. However it's a general legal principle too, that a business or transaction's only goal cannot be to achieve tax benefit, there always must be a legitimate commercial motivation. So that isn't legitimate, if the only reason of settling down or establishing headquarters in a specific country, because it has a smaller tax burden, but it shouldn't be objectionable, if during the planning the company is having a chance to - within the limits of legality – to involve small tax rate countries into their business structure.

If you're interested in this topic or if you have any additional questions about setting up or managing an offshore company, please contact us, our legal experts would be pleased to help you.

Contact

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About Accace

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Accace offices are located in Czech Republic, Hungary, Romania, Slovakia, Poland, Ukraine and Germany. Locations in other European countries and globally are covered via Accace's trusted partners network.

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